

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
Nora Mead Brownell, Joseph T. Kelliher,
and Suedeem G. Kelly.

Conectiv Energy Supply, Inc.

Docket No. ER05-121-000

ORDER ACCEPTING AND SUSPENDING POWER PURCHASE AGREEMENT,
SUBJECT TO REFUND, AND ESTABLISHING HEARING PROCEDURES

(Issued December 30, 2004)

1. In this order, we will accept for filing a power purchase agreement (PPA) between Conectiv Energy Supply, Inc. (CESI) and its affiliate, Delmarva Power & Light Company (Delmarva), suspend it for a nominal period, to become effective on January 1, 2005, as requested, subject to refund, and establish hearing procedures. This order benefits customers by assuring sales among affiliates adhere to the Commission's standards for evaluating market-based rate affiliate sales resulting from RFP processes.

I. Background

2. On October 29, 2004, CESI filed the instant application under section 205 of the Federal Power Act.¹ CESI states that as part of a Request for Proposal (RFP) process, CESI has been selected to supply Delmarva with full requirements service to fulfill Delmarva's Virginia retail customer load obligation. For this reason, CESI seeks Commission authorization to make wholesale power sales to its affiliate, Delmarva, pursuant to the PPA. CESI requests an effective date of January 1, 2005.

3. CESI and Delmarva are both wholly-owned subsidiaries of Pepco Holdings, Inc. CESI is a power marketer that owns no generation, transmission or distribution facilities, but has authority to sell power and energy at market-based rates.² Delmarva is a franchised electric utility that has transferred functional control of its transmission system to PJM Interconnection, L.L.C. (PJM). Delmarva is required to provide standard offer service to any customer that does not choose an alternate supplier under the Virginia

¹ 16 U.S.C. § 824d (2000).

² See *Conectiv Energy Supply, Inc.*, 83 FERC ¶ 61,090 (1998), and *Conectiv Energy Supply, Inc.*, 91 FERC ¶ 61,076 (2000), *order on reh'g*, 94 FERC ¶ 61,068 (2001)

Electric Utility Restructuring Act until 2010.³ Delmarva provides standard offer service at fixed prices that are established by the Virginia Commission based on Delmarva's cost of purchased power.

4. CESI states that on August 27, 2004, the representatives of Delmarva met with senior staff members of the Virginia Commission to discuss the power purchase contract, other documentation and the procedure that would be used to select the wholesale power supplier for Delmarva's retail customer load after December 31, 2004.⁴ During that meeting, the Delmarva representatives described the RFP processes that had been used in Maryland and in the District of Columbia and suggested that those RFP processes might also be used in Virginia. Upon learning that the Virginia Commission would not be opening a formal proceeding to establish an RFP process for Virginia, Delmarva commenced implementation of an RFP process that CESI states was virtually the same as those that were used in Maryland and the District of Columbia.⁵

5. Subsequently, Delmarva issued its RFP (Delmarva RFP), notifying sixty-two potential suppliers by letters dated September 2, 2004, that it would be seeking bids to provide 97.5 MW of full requirements service for its Virginia retail customer load for a term of seventeen months, beginning January 1, 2005.⁶ Nine power suppliers qualified to bid. CESI states that the power purchase contract terms and conditions were established prior to bidding and because such terms and conditions were non-negotiable, bidders competed on the basis of price only. On October 6, 2004, Delmarva received seven bids from well-known energy suppliers. It awarded the power purchase contract to CESI, the lowest bidder, on October 7, 2004.

6. CESI states that Delmarva filed an application with the Virginia Commission seeking approval of the PPA under the Virginia Affiliates Act and seeking retail rate adjustments that reflect the prices that Delmarva will pay to CESI as the low price bidder. The Virginia Commission set a public hearing for these filings to convene on March 16,

³ See § 56-576 et. seq. of the Code of Virginia.

⁴ CESI's obligation to meet Delmarva's Virginia customer requirements under a master agreement that provided for CESI to sell power to Delmarva Power required to meet its obligation as the provider of last resort (PLR transaction) is scheduled to terminate on December 31, 2004.

⁵ The RFP process ultimately adopted in Maryland was reviewed by the Commission in *Allegheny Energy Supply Company, LLC*, 108 FERC ¶ 61,082 (2004) (*Allegheny*).

⁶ CESI states that this contract term was used to synchronize Delmarva's power purchase contracting process with the PJM annual planning periods, which begin on June 1 and extend through May 31 of the next calendar year.

2005. The Virginia Commission further permitted the implementation of an interim fuel rate, subject to refund, on and after January 1, 2005, applicable on a uniform basis to all of Delmarva's Virginia jurisdictional customers.⁷

II. Notice of Filing and Pleadings

7. Notice of CESI's filing was published in the *Federal Register*,⁸ with protests and motions to intervene due on or before November 19, 2004. None were filed.

III. Discussion

8. As noted above, CESI asks the Commission to accept a PPA allowing CESI to make sales to its franchised electric utility affiliate, Delmarva. In order to meet the Commission's requirements for sales between affiliates, CESI offers evidence that the RFP process applied to this PPA satisfies the standards announced by the Commission in *Allegheny* for determining when an RFP satisfies the Commission's concerns regarding affiliate abuse.⁹

9. The Commission has stated that, in cases where affiliates are entering into market-based rate sales agreements, it is essential that ratepayers be protected and that transactions be above suspicion in order to ensure that the market is not distorted.¹⁰ The Commission has approved affiliate sales resulting from competitive bidding processes after the Commission has determined that, based on the evidence, the proposed sale was a result of direct head-to-head competition between affiliated and competing unaffiliated suppliers.¹¹ When an entity presents this kind of evidence, the Commission has required

⁷ See *Public Order of the Virginia State Corporation Commission, Order for Notice and Hearing*, CASE NOS. PUE-2004-00124 PUE-2004-00125, issued November 17, 2004. Delmarva's application with the Virginia Commission discloses, on a confidential basis, the prices that were bid by other prospective suppliers. Delmarva will disclose the identity of the bidders to the Virginia Commission and its staff, if requested, as provided in the Confidentiality Agreement that is part of the Delmarva RFP.

⁸ 69 Fed. Reg. 65,422 (2004).

⁹ *Allegheny*, 108 FERC ¶ 61,082.

¹⁰ See *Boston Edison Co. Re: Edgar Electric Energy Co.*, 55 FERC ¶ 61,382 at 62,167 (1991) (*Edgar*).

¹¹ See *Connecticut Light & Power Company and Western Massachusetts Electric Company*, 90 FERC ¶ 61,195 at 61,633-34 (2000); *Aquila Energy Marketing Corp.*, 87 FERC ¶ 61,217 at 61,857-58 (1999); *MEP Pleasant Hill, LLC*, 88 FERC ¶ 61,027 at 61,059-60 (1999); *Edgar*, 55 FERC ¶ 61,382 at 62,167-69.

assurance that: (1) a competitive solicitation process was designed and implemented without undue preference for an affiliate; (2) the analysis of bids did not favor affiliates, particularly with respect to non-price factors; and (3) the affiliate was selected based on some reasonable combination of price and non-price factors.¹²

10. In *Allegheny*, the Commission provided guidance as to the standards the Commission will use to evaluate whether an RFP such as the one in the instant proceeding meets the *Edgar* criteria. As the Commission stated, the underlying principle when evaluating an RFP under the *Edgar* criteria is that no affiliate should receive undue preference during any stage of the RFP. The Commission indicated that the following four guidelines will help the Commission determine if an RFP satisfies that underlying principle:

- a. Transparency: the competitive solicitation process should be open and fair.
- b. Definition: the product or products sought through the competitive solicitation should be precisely defined.
- c. Evaluation: evaluation criteria should be standardized and applied equally to all bids and bidders.
- d. Oversight: an independent third party should design the solicitation, administer bidding, and evaluate bids prior to the company's selection.

11. As discussed above, Delmarva commenced implementation of an RFP process that was similar to those used in Maryland and the District of Columbia. On September 7, 2004, Delmarva activated a website¹³ which provided detailed information to prospective bidders. The PPA terms and conditions were established prior to bidding and because such terms and conditions were non-negotiable, bidders competed on the basis of price only.

12. To be eligible to submit bids, potential suppliers were required to submit: an expression of interest; a signed confidentiality agreement; documentation that the potential supplier is a member of PJM and a qualified market buyer and market seller in good standing; documentation that the potential seller is authorized at the federal level to make wholesale sales of energy, capacity, and ancillary services at market-based rates; and submission of a credit application and associated financial information.¹⁴ By pre-qualifying potential bidders before the bid process began, CESI states that Delmarva

¹² *Edgar*, 55 FERC ¶ 61,382 at 62,168.

¹³ (www.conectiv.com/varfp).

¹⁴ *Delmarva RFP* at 6-7 (October 4, 2004).

eliminated the need to evaluate bidders based on non-price factors, thereby allowing bid selection based solely on price. An entity that had any deficiencies in its submittal was notified by Delmarva by email. The entity then had the opportunity to correct deficiencies, if resubmitted in a timely manner.

13. Bids were submitted in standardized Bid Form Spreadsheets. For each bid submitted to Delmarva, potential suppliers were allowed to input bid blocks information, price period within contract term, price quote for bid block offered, volume weighing factors, discount factors, load weighted prices, discounted price for evaluation purposes, tag number, and complete/incomplete flag. Bidders could submit as many different bids as they chose. Bidders were not allowed to submit bids with terms other than those set by Delmarva in the RFP.

14. The winning bidder was selected on the basis of a single, calculated price for each individual bid. This single parameter used to compare all bids is called Discounted Average Term Price (DATP). The winning bidder, CESI, was selected based on DATP alone.

15. Bids submitted were binding. The winning bidder received the actual price and volume quotes entered on their Bid Form Spreadsheet. Bidders were required to accept the terms of the pro forma Full Requirements Service Agreement. Winning bidders were not permitted to revise prices or any other terms and conditions of their supply contract.

16. CESI explains that an independent third party did not design the solicitation, administer bidding or evaluate bids prior to Delmarva's selection. However, CESI states that it believes this RFP process meets the Commission's oversight principle because it utilized the documentation and process adopted through the collaborative process in Maryland and approved by the Commission in the *Allegheny* order.¹⁵ CESI submits that since that same RFP process as was adopted in Maryland was used here, there can be no assertion that CESI had any undue preference in the design phase of the competitive solicitation, including, but not limited to, the form of the PPA and the standards for qualifying bidders. CESI contends that it was not necessary to use an independent third party to evaluate bids in this case since the process was standardized such that Delmarva's only role was to select the lowest price submitted by the bidders.

17. CESI further states that, in an effort to mitigate wholesale suppliers' exposure to volumetric risk associated with non-residential customer migration, the Virginia Commission provided that certain restrictions will apply to customers who, having left standard offer service, then return to standard offer service. This is outlined in the RFP. According to CESI, this mechanism allowed bidders to make offers without considering

¹⁵ *Allegheny*, 108 FERC ¶ 61,082.

the risk of standard offer service demand shifts. However, at this time, no retail customers within Delmarva's Virginia service area are being served by a competitive service provider. Delmarva's RFP also stated that Delmarva will not adjust the prices paid to the winning bidder during the procurement term of the transaction due to changes in PJM or other market factors with a corresponding, contemporaneous change in retail rates. CESI states that, by statute, Delmarva may not request that the Virginia Commission change its retail rates more than one time in a twelve-month period.

18. CESI acknowledges in its filing that an independent third party did not design the solicitation, administer bidding or evaluate bids prior to Delmarva's selection. Because the RFP does not meet the oversight principle as announced in *Allegheny*, the Commission is unable to determine that no affiliate received undue preference during any stage of the RFP. For example, prospective bidders were required, among other things, to submit a credit application and associated financial information. Without independent third-party oversight, such criteria could be used to limit potential competitors from submitting bids. On this basis, the Commission's preliminary analysis indicates that the PPA between CESI and Delmarva that resulted from the Delmarva RFP has not been shown to be just and reasonable, and may be unjust, unreasonable, unduly discriminatory or preferential or otherwise unlawful. CESI's application raises issues of material fact that cannot be resolved based on the record before us and are more appropriately addressed in the hearing ordered below.

19. Therefore, we will accept the PPA for filing, suspend it for a nominal period, to become effective on January 1, 2005, as requested, subject to refund, and establish hearing procedures.

20. The hearing should determine: (1) whether in the design and implementation of the Delmarva RFP unduly preferred its own affiliate, CESI; and (2) whether the credit criteria and analysis unduly favored CESI.

The Commission orders:

(A) The PPA is hereby accepted for filing, suspended for a nominal period, to become effective on January 1, 2005, as requested, subject to refund, as discussed in the body of this order.

(B) Pursuant to the authority contained in and subject to the jurisdiction conferred upon the Federal Energy Regulatory Commission by section 402(a) of the Department of Energy Organization Act and by the Federal Power Act, particularly sections 205 and 206 thereof, and pursuant to the Commission's Rules of Practice and Procedure and the regulations under the Federal Power Act (18 C.F.R., Chapter I), a public hearing shall be held concerning the justness and reasonableness of the PPA between CESI and Delmarva that resulted from the Delmarva RFP.

(C) A Presiding Judge, to be designated by the Chief Judge, shall, within fifteen (15) days of the date of the Presiding Judge's designation, convene a prehearing conference in these proceedings in a hearing room of the Federal Energy Regulatory Commission, 888 First Street, N.E., Washington, DC 20426. Such conference shall be held for the purpose of establishing a procedural schedule. The Presiding Judge is authorized to establish procedural dates, and to rule on all motions (except motions to dismiss) as provided in the Commission's Rules of Practice and Procedure.

By the Commission. Commissioner Kelliher dissenting with a separate statement attached.

(S E A L)

Linda Mitry,
Deputy Secretary.

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Conectiv Energy Supply, Inc.

Docket No. ER05-121-000

(Issued December 30, 2004)

Joseph T. KELLIHER, Commissioner *dissenting*:

I dissent from the decision in this order to set the power purchase agreement (PPA) between Conectiv Energy Supply, Inc. (Conectiv) and its affiliate, Delmarva Power & Light Company (Delmarva) for hearing.

The Commission has explained that its concern in cases where affiliates are entering into market-based rate sales agreements is that ratepayers be protected and that transactions be above suspicion in order to ensure that the market is not distorted.¹⁶ The Commission has approved affiliate sales resulting from competitive bidding processes where the Commission determined that the proposed sale was the result of direct head-to-head competition between affiliated and competing unaffiliated suppliers.¹⁷ In *Allegheny Energy Supply Co., LLC*, 108 FERC ¶ 61,082 at P22 (2004)(*Allegheny*) the Commission stated that “the underlying principle when evaluating an RFP under the *Edgar* criteria is that no affiliate should receive undue preference during any stage of the RFP” and outlined four “guidelines,” as opposed to requirements, to “help” the Commission determine if an RFP satisfies that underlying principle. *Allegheny* did not indicate that failure to meet all four “guidelines” mandated a hearing.

Here, the Commission’s concern appears to be with only one of the four guidelines:

¹⁶ *Boston Edison Co. Re: Edgar Electric Energy Co.*, 55 FERC ¶ 61,382 at 62,167 (1991)(*Edgar*).

¹⁷ See *Connecticut Light & Power Co. and Western Massachusetts Electric Co.*, 90 FERC ¶ 61,195 at 61,633-34 (2000); *Aquila Energy Marketing Corp.*, 87 FERC ¶ 61,217 at 61,857-58 (1999); *MEP Pleasant Hill, LLC*, 88 FERC ¶ 61,207 at 61,059-60 (1999); *Edgar*, 55 FERC at 62,167-69.

oversight by an independent third party. However, the RFP process used here was the same process that had been reviewed and approved by the Commission in *Allegheny*. Moreover, in this instance, sixty-two potential suppliers were notified, nine power suppliers qualified to bid, and seven bids were submitted. Significantly, no protests were filed. In these circumstances, it is reasonable to find the absence of undue preference. For that reason, I would accept the PPA rather than set it for hearing.

Finally, I emphasize my view that the four criteria set forth in *Allegheny* constitute guidelines the Commission will consider on a case-by-case basis in evaluating an RFP in an affiliate situation rather than a “bright-line” test that must be satisfied to avoid a hearing.

Joseph T. Kelliher